

SOUTH FLORIDA WATER MANAGEMENT DISTRICT



Audit of the Everglades Construction Project Cooperative Agreements

Audit #01-14

**Prepared by
Office of Inspector General**

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Mr. Michael Collins, Member
Mr. Patrick J. Gleason, Member

Re: Final Report – Audit of the
Everglades Construction Project
Cooperative Agreements #01-14

This audit was performed pursuant to the Inspector General's authority set forth in Chapter 20.055, F.S. The audit focused on management of ECP projects carried out through two cooperative agreements with external organizations. The objectives of the audit were substantiating expenditure reimbursements, assessing compliance with agreement terms, and evaluating whether best business practices were followed in administering these projects. This report was prepared by Tim Beirnes.

Sincerely,

Allen Vann
Inspector General

Enclosure

c: Henry Dean

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TABLE OF CONTENTS

INTRODUCTION	1
OBJECTIVES, SCOPE AND METHODOLOGY	3
RESULTS IN BRIEF.....	4
FINDINGS AND RECOMMENDATIONS	6
REVIEW OF COSTS	6
298 Districts.....	6
Closter Farms.....	9
Conditions Affecting Cost.....	10
REVIEW OF ACCOUNTING RECORDS AND PAYMENT PROCESS.....	12
COMPLIANCE WITH CONTRACTUAL REQUIREMENTS.....	13
EVERGLADES RESTORATION PROJECT FUNDING ISSUES	14
APPENDICES	
Appendix I - Schedule of Actual and Estimated Cost for 298 District Projects and Budget Shortfall	
Appendix II - 298 District's Responses	
Appendix III - Closter Farms' Responses	

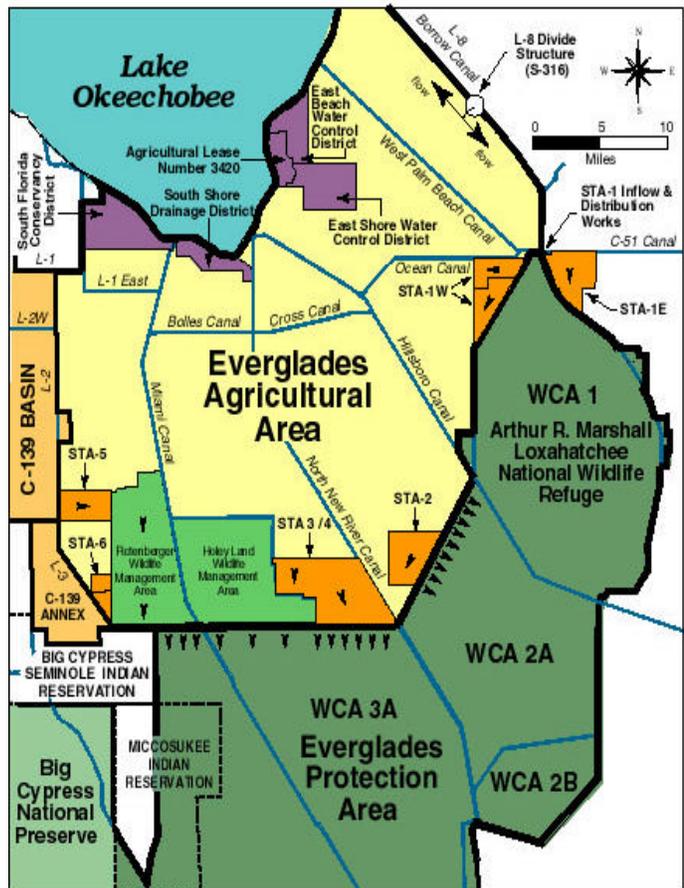
INTRODUCTION

This report details the results of our audit of the South Florida Water Management District's (the District) cooperative agreements with four special drainage districts (298 Districts) and the lessee of agricultural lease number 3420 (Closter Farms) under the Everglades Construction Project (ECP). The audit's primary objectives were to substantiate expenditures submitted to the District for reimbursement, determine whether agreement provisions were complied with, and that best business practices were employed to obtain the greatest value for the taxpayers.

The Everglades Forever Act's (EFA) Conceptual Design Document provides for reconfiguring the drainage of the 298 Districts' and Closter Farms' areas to divert water currently flowing into Lake Okeechobee into the Storm-water Treatment Areas STA's. These projects were completed directly by the 298 Districts and Closter Farms under cooperative agreements with the District. Funding for the projects was provided from the Everglades Trust Fund, as required by the EFA.

The five basins are part of the Everglades Agricultural Area (EAA) and cover approximately 32,081 acres along the south and east shore of Lake Okeechobee. They are situated primarily in Palm Beach County. Historically, these districts have discharged some of their runoff into Lake Okeechobee.

The 298 Districts are special drainage districts operating under the authority of Florida Statutes Chapter 298. Daily activities of these four special districts are performed by a common administrator and small staff located in Bell Glade, Florida. Hence, a single cooperative agreement was executed concurrently with all the following four 298 Districts:



- The South Florida Conservancy District
- The South Shore Drainage District
- The East Beach Water Control District
- The East Shore Water Control District

Articles II, IV and V of the 298 District Agreement specify the following primary obligations of the District and the 298 Districts:

- Article II, Section A states: "The 298 Districts, upon execution of the contract, shall expeditiously design and construct the Project applying those procedures usually applied to 298 District projects, pursuant to applicable laws, regulations and policies."
- Article II, Section B states: "The 298 Districts shall afford the District the opportunity to review and comment on the solicitations for all construction and engineering contracts, including relevant plans and specifications, prior to the 298 Districts' issuance of such solicitations. The 298 Districts shall not initiate further design work, permitting activity, other projects-related activity or issue a solicitation for a construction contract until the District has confirmed in writing its ability to fund the Agreement. The contents of solicitations, award of contracts, execution of contract modifications, issuance of change orders, resolution of contract claims, and performance of all work on the Project (whether the work is performed under contract or by 298 Districts personnel) shall be exclusively within the control of the 298 Districts but the 298 Districts shall consider in good faith the comments of the District related thereto."
- Article II, Section D states: "The 298 Districts shall solely operate, maintain and control the Project."
- Article IV, Section A states: "The 298 Districts shall be reimbursed for project costs retroactive to May 3, 1994, the date of passage of the Everglades Forever Act."
- Article V, Section A states: "The 298 Districts shall set up a single interest bearing escrow account for funds to be received under this agreement designating an authorized agent to withdraw from the account. The agent may only withdraw funds from this account for payments to the individual 298 Districts for the purpose of paying for their contractual services under this agreement. District approval is not required for disbursing funds from the account by the 298 Districts for disbursements made to their respective contractors. The District shall be provided a copy of a monthly escrow

trust account reporting all detail financial activity to include disbursements, reimbursements, interest and reasonable trustee fees . . ."

A separate agreement was executed with Closter Farms - a private enterprise. Similar provisions are included in the Closter Farms contract, except that it did not require affording the District the opportunity to review and comment on the solicitation for engineering contracts and did not require establishing an escrow account.

OBJECTIVES, SCOPE AND METHODOLOGY

The objectives of the audit were to substantiate expenditure reimbursements, assess compliance with agreement terms, and evaluating whether best business practices were followed in administering the projects.

The audit scope included the period from inception to July 31, 2001, for the following agreements:

- Cooperative Agreement Between the South Florida Water Management District and the East Shore Water Control District, East Beach Water Control District, South Shore Drainage District and South Florida Conservancy District (Contract Number C-E006).
- Contract between the South Florida Water Management District and Closter Farms, Inc. (Contract Number C-E003)

Methodology included the following:

- Reviewing contract files maintained by Contract Administrators and Project Managers,
- Interviewing District personnel, vendors, grantees, and others as deemed necessary,
- Physically observing the project and meeting with 298 Districts' and Closter Farms' representatives,
- Performing other procedures as deemed necessary.



RESULTS IN BRIEF

Review of Costs

The 298 Districts & Closter Farms expended a combined total of \$15.8 million. Our review of costs incurred for these projects indicated that all costs were allowable and allocable in accordance with the terms of the agreements. However our analysis of the costs incurred suggest that there were opportunities to reduce professional fees incurred for engineering, appraisal and legal fees.

Overall, combined professional service fees for the 298 Districts were 23% of total infrastructure cost. Closter Farms professional fees were 54% of construction cost of which half was for legal fees. Engineering fees were only slightly higher than amounts based on benchmarks we identified in a prior audit that addressed reasonableness of engineering cost.

Many legal services provided to Closter Farms entailed project manager type activities that could have been provided by an engineering firm or an (SFWMD) District staff for substantially less. Land appraisal services incurred by the 298 District's could also have been obtained for 25% to 35% less, providing a savings of approximately \$60,000 to \$90,000. The agreements obligated the SFWMD with the responsibility to pay for the projects without the authority to manage cost. Future cooperative agreements should provide for stronger District control and more active participation by District staff in business decisions.

Review of Accounting Records and Payment Process

Vendor payments were made in accordance with executed contracts and no questioned costs were identified. The 298 Districts' and Closter Farms accounting records provided a good audit trail to substantiate reimbursed expenditures; however, District staff did not maintain adequate supporting documentation for reimbursements made during the first two years of the contract for the 298 District's. The condition appears to have resulted from inadequate attention to the contract due to staff's attention being focused on other higher priority ECP projects. During the audit, the 298 District provided us with all the supporting documentation, which sufficiently supported the earlier reimbursed amounts.

Compliance with Contractual Requirements

Overall, contract provisions were complied with and the 298 Districts' and Closter Farms' records were sufficient to substantiate reimbursed expenditures. However, District staff was not afforded the opportunity to review and comment on solicitations for engineering contracts prior to the issuance of such solicitations, as required by the 298 District's contract, because professional services were procured through appointment instead of competitive solicitations. Lower fees likely could have been obtained if professional services would have been procured through a competitive solicitation process.

Everglades Restoration Project Funding Issues

An additional \$8.4 million is needed to complete the remaining 298 Districts' projects. This shortfall is due primarily to following dated budget estimates incorporated into the Everglades Protection Project Conceptual Design Document. While savings have been realized through value engineering, the 298 Districts' and Closter Farms projects are currently estimated to cost approximated \$12.7 million more than the original \$11.5 million original estimate.

The current ECP financial schedules show a total projected deficit for the entire ECP of almost \$21 million when the project is completed in Fiscal Year 2006; however, this does not include more than \$7 million needed to fund the two remaining 298 District projects. A means is necessary to fully fund the project

Currently ECP financial schedules reflect that collection of the 1/10 Mill Ad Valorem Tax will be terminated when total revenues from this source reaches \$279 million - an amount based on the February, 15 1994 revenue projection schedule in the Conceptual Design Document. The Office of Counsel reviewed this issue in May 2000 and determined that the EFA does not cap revenues from the 1/10th Millage Ad Valorem Tax (1/10th Mill).

In the event that other revenue sources are not identified and sufficient additional savings are not realized on current project costs including operations and maintenance, we recommend that staff obtain Governing Board approval for assessing the 1/10th Mill Ad Valorem Tax for the (short) length of time necessary to generate sufficient revenue to cover the current projected budget deficit and fund the remaining 298 Districts' projects.

FINDINGS AND RECOMMENDATIONS

REVIEW OF COSTS

Our review of costs incurred for these projects indicated that all costs were allowable and allocable in accordance with the terms of the agreements. However our analysis of the costs incurred suggest that there were opportunities to reduce professional fees incurred for engineering, appraisal and legal fees. Details for each agreement are presented separately below.

298 Districts

Professional service costs compared to tangible construction and land acquisition expenditures for the 298 Districts are reflected in the following table accompanied with notes on the following page that contains our discussion and analysis of each cost component:

<i>Description</i>	<i>East Shore</i>	<i>East Beach</i>	<i>Total Cost</i>	<i>Notes</i>
Land Acquisition	\$ 634,616	\$ 883,073	\$ 1,517,689	(1)
Construction Cost	5,679,520	4,208,968	9,888,488	(2)
Total Land & Construction	\$6,314,136	\$ 5,092,041	\$ 11,406,177	
Professional Services:				
Engineering - Design & Constr. Managment	\$ 728,886	\$ 1,019,310	\$ 1,748,196	(3)
Engineering- Other	173,923	157,167	331,090	(4)
Legal	114,742	146,541	261,283	(5)
Appraisals	45,150	223,110	268,260	(6)
Subtotal	\$ 1,062,701	\$ 1,546,128	\$ 2,608,829	
Total Cost	\$7,376,837	\$ 6,638,169	\$ 14,015,006	

Notes

- (1) Land acquisition includes the cost of acquiring various types of land interests including easements and other right-of-way interests. Acquisitions primarily related to land required for canal right-of-ways.

- (2) Construction cost involved primarily building pump stations, digging new canals, enlarging existing canals, and installing crossing structures. Construction contracts were solicited through the sealed bid process and were awarded to the lowest responsive bidder.
- (3) Engineering Design & Construction Management includes the cost of drafting the detail design, preparing specifications, and monitoring construction activities during the construction phase. These costs as a percentage of construction cost were 13% for the East Shore Water Control District, 24% for the East Beach Water Control District.

During our past audit(s) of the District's ECP project¹, we used two engineering cost benchmarks to evaluate the reasonableness of engineering cost incurred by ECP as a percentage of our construction costs. The first benchmark was the Conceptual Design Document (CDD) which fixed the percentage at 13.5%. The second benchmark we used was the PSMJ Fee Survey² at 12%.

The engineering services for the East Shore Drainage District appears in line with the benchmarks; however, the East Beach Water Control District costs at 24% is higher than the benchmarks. However, \$155,490 in engineering services expense was incurred due to construction delays and performance issues by one of East Beach Water Control District's construction contractors. These costs may be recoverable through the liquidated damages provisions in the contract and performance bond.

¹ *Audit of the Everglades Construction Project Procurement Process # 97 -15*, dated June 3,1998. Also see Follow-up Report on Everglades Construction Project Design and Construction Management Cost Issues, Report # 00 -14, dated August 15, 2000.

² Our previous audit also compared engineering cost to industry averages based on the *Design Services Fee Survey*, 12th Edition, Published by PSMJ Resources, Inc. (the "Fee Survey"). PSMJ Resources, Inc. is an international provider of strategic planning, management, marketing information, and services for the design and construction industries. The Fee Survey was derived from a survey of 261 engineering firms and is used by the construction and engineering community.

- (4) Other Engineering costs, not suited to inclusion under the benchmark analysis, include the following services (based on information provided by the 298 Districts):
- \$174,632 for preliminary design work performed prior to commencing with the detail design.
 - \$81,514 for a value engineering study and redesign work, which resulted in reducing land acquisition and construction cost by approximately \$3 million.
 - \$74,944 for non-design services such as surveying, geotechnical, services related to right-of-way acquisitions, etc.
- (5) Legal fees were 2% of land and construction cost for the combined projects. Legal fees included services related to executing the agreement between the SFWMD and the 298 Districts, permitting assistance, contracting issues, and other legal consultation. Approximately \$42,929 in legal expense was incurred due to the aforementioned construction delays and performance issues by one of the construction contractors for the East Beach Water Control District. These costs may be recoverable through the liquidated damages provisions in the contract and performance bond.
- (6) Appraisal costs were incurred to establish the fair market value of land interest required for the projects. These costs as a percentage of Land Acquisitions were 7% for the East Shore Water Control District compared to 25% for the East Beach Water Control District. According to our Chief Appraiser, lower fees could have been negotiated for land appraisal services. We asked the Chief Appraiser to review the scope of work performed by the 298 Districts' appraiser to determine what we would have expected to pay if it we negotiated for the same services. In his opinion, these services could have been procured for 25% to 35% less - approximately \$60,000 to \$90,000 less than the \$268,000 actually paid. This could have been accomplished through more competitive selection processes and following other standard procedures that the District follows to ensure equitable and fairly priced services. In fact, the District could have provided assistance to the 298 Districts to facilitate obtaining these services.

Closter Farms

Closter Farms' professional fees were 54% of construction cost. Professional service fees compared to tangible costs for Closter Farms are shown in the following table.

Closter Farms - Total Cost			
Description	Total Estimated Cost	Percentage of Construction Cost	Notes
Land Acquisition	-0-		(1)
Construction Cost	\$ 1,001,294		(2)
Professional Services:			
Engineering-Design & CM	148,727	15%	(3)
Engineering - Other	106,546	10%	(4)
Legal	270,000	27%	(5)
Accounting	16,010	2%	(6)
Subtotal	\$ 541,283	54%	
Total Cost	\$ 1,542,577		

Notes

- (1) No direct land costs were incurred for Closter Farms; however, legal fees were incurred related to securing an easement.
- (2) Construction cost involved primarily building pump stations, digging new canals, enlarging existing canals, and installing crossing structures. Construction contracts were solicited through the sealed bid process and were awarded to the lowest responsive bidder.
- (3) Engineering Design & Construction Management includes the cost of drafting the detail design, preparing specifications, and monitoring construction activities during the construction phase. These costs as a percentage of construction cost were 15%. Using our benchmarks from our previous audits (see note 2 on page 7) 13.5% from the ECP Conceptual Design Document (CDD) and the 12% from the PSMJ Fee Survey, suggest that engineering cost for Closter Farms was just above the benchmark.

(5) Other Engineering costs included the following services:

- \$18,150 for topographic survey services.
- \$22,457 conceptual development of diversion plan.
- \$59,101 for permit support and M/WBE coordination.
- \$6,838 Other non-design and non-construction management services.

(5) Legal fees were 27% of construction costs compared to the legal fees for the 298 Districts' projects, which were only 1.8%. Legal fees involve services related to executing the agreement between the SFWMD and Closter Farms, permitting assistance, contracting issues, and other legal consultation. The services provided also entailed project management type activities. Although no benchmarks exist to evaluate these costs, legal fees comprising a quarter of the projects' hard costs appears excessive.

(6) An accounting firm was hired to provide services to satisfy certain contractual requirements of the agreement. These services include preparing monthly invoices, quarterly accounting reports, attending certain meetings, and preparing final project accounting.

Conditions Affecting Costs

The following conditions affected the cost of professional service fees:

- The District was not involved in either soliciting or negotiating contracts for professional services. Fees do not appear to have been aggressively negotiated for some professional services. Both organizations engaged their own firms prior to executing a formal agreement with the District, and costs were permitted to be incurred for two to three years by some firms before the agreements were executed. By that time, these business arrangements had already been well established and the project budgets were determined based on fee arrangements that had already been established.
- Higher priced professionals were used to provide services that required skills that could have been performed by lower priced professionals.

Based on a review of legal invoices for Closter Farms, many legal services essentially entailed project management type activities. District staff or an engineering firm could have provided many of these services for substantially less than the \$190 to \$200 per hour charged by the law firm.

- The agreements with the 298 Districts and Closter Farms obligated the SFWMD with the responsibility to pay for the projects without the authority to manage cost. This resulted in a business environment that was not accommodating to controlling costs.

Recommendation

1. **For the two additional projects that are scheduled for the 298 Districts, Everglades Construction Project management staff should provide assistance with the award and administration of contracts and help control costs.**

Management Response:

The District will pursue amending the current agreement with the 298 Districts to provide for the ECP staff to be more meaningfully involved in the specific areas of design review and construction management.

Responsible Division: ECP Department

Estimated Completion Date: December 2003



REVIEW OF ACCOUNTING RECORDS AND PAYMENT PROCESS

Vendor payments were made in accordance with executed contracts and no questioned costs were identified. The 298 Districts' and Closter Farms' accounting records provided a good audit trail to substantiate reimbursed expenditures. However, District staff did not receive, review, and maintain adequate supporting documentation for reimbursements made during the first two years of the 298 District contract. Most of the cost during this period was for legal and engineering services for which summary invoices were provided for amounts paid; however, documentation was not provided to support the charges from the vendors. Under reimbursement contract arrangements such as these, project management/internal control practices should have required obtaining and verifying sufficient supporting documentation before disbursing the funds.

The condition appears to have resulted from inadequate attention to the contract due to staff's attention being focused on other higher priority ECP projects. Proper documentation was received and reviewed by District staff for reimbursements made subsequent to (monthly) invoice number 22. This improvement coincided with the contract being assigned to a new District Contract Administrator.

The lack of appropriate documentation lengthened and extended the scope of this audit. Our Office requested the 298 Districts provide additional supporting documentation. The 298 Districts did provide us with all the missing supporting documentation, which sufficiently supported the reimbursed amounts. Additionally, we examined cancelled checks to support these expenditures without exception.

Recommendation

- 2. Everglades Construction Project Implementation staff should ensure that adequate supporting documentation is obtained and reviewed for all disbursements of funds from the inception of any project.**

Management Response:

Everglades Construction Project Implementation staff will continue to improve the invoice processing review and documentation consistent with the agreement modifications noted in Recommendation #1 for design review and construction management.

Responsible Division: ECP Department

Estimated Completion Date: December 2003

COMPLIANCE WITH CONTRACTUAL REQUIREMENTS

Overall, contract provisions were complied with and the 298 Districts' and Closter Farms' records were sufficient to substantiate reimbursed expenditures. However, District staff was not afforded the opportunity to review and comment on solicitations for engineering contracts prior to the 298 Districts' issuance of such solicitations as required in Article II, Section B of the respective cooperative agreements (See Background, page 2). Professional services were procured through appointment for firms the organizations had existing business relationships with instead of separate competitive solicitations for the Everglades projects. However, the 298 Districts' engineering firm was selected through the Consultants Competitive Negotiation Act (CCNA) process in 1992 to serve as the 298 Districts' engineer.

Both organizations engaged their own engineering firms prior to executing a formal agreement between the District and the 298 Districts/Closter Farms and selection of the firms was established prior to executing the Cooperative Agreement with the District. In both situations, the appointed firms had previous involvement in the project during the conceptual design phase. Better fees would likely have been achieved if professional services had been procured through a competitive solicitation process.

Recommendation

- 3. Everglades Construction Project Implementation staff should proactively monitor compliance with contract provisions.**

Management Response:

The amendment of the agreement (as identified in Recommendation #1) will address the overall intensity of the ECP staff monitoring of the project for compliance with contract provisions.

Responsible Division: ECP Department

Estimated Completion Date: Continuous through December 2003

EVERGLADES RESTORATION PROJECT FUNDING ISSUES

Our analysis comparing the current budget estimates for the entire diversion project to the original Conceptual Design Document (CDD) budget (see Appendix, page 18) indicates that the total estimated cost for these projects are approximately \$24.2 million. The original CDD budget was \$11.5 million, however, \$15.8 million has already been expended for two of the four 298 Districts' projects (including Closter Farms and \$223,000 expended on the other two 298 District projects prior to suspending work due to funding issues). An additional \$ 8.4 million will be needed to complete the South Shore Drainage District and South Florida Conservancy District projects. Most of the overrun is due to following dated budget estimate incorporated into the CDD and to some degree, the higher than anticipated costs of the already completed diversion projects.

The following table summarizes the sources of projected revenues for ECP capital cost from 1994 through 2006:

Revenue Source	Estimated Revenue
Ad Valorem Tax - 1/10 mill	\$ 279,000,000
Federal Contribution (In-Kind)	190,249,000
Agricultural Privilege Tax	148,641,973
State and Other Revenue	<u>99,128,623</u>
Total	<u>\$ 717,019,596</u>

The current ECP financial schedules reflect a total projected deficit for the entire ECP of \$20.8 million through completion in fiscal year 2006.³ The projected deficit does not include the \$ 7.1 million of the \$8.4 million needed to complete the two remaining 298 Districts' projects; thus, the projected deficit would be \$27.9 million if these projects were included. Consequently, a funding source is necessary to offset this projected deficit and provide the necessary funds to complete all the projects. The deficit results from an imbalance between revenues and expenditures as reflected by District staff in the ECP Financial Statements. Adjusting the projected revenues can easily rectify the shortfall. The Financial statements assume that collection of the 1/10 Mill Ad Valorem Tax⁴ will end when total revenues from this source reach

³ The majority of the funding shortfall resulted from higher land acquisition costs.

⁴ The Everglades Forever Act specifies that (not more than) one-tenth of a mill (.100) of the District's Okeechobee Basin millage be dedicated to the Everglades Construction Project.

\$279 million. This assumption is based upon outdated revenue projection schedules in the original ECP Conceptual Design Document.

The 1/10th Mill Ad Valorem Tax actual revenues for prior fiscal years and estimated revenues for future fiscal years are shown in the following table:

<i>Fiscal Year</i>	<i>Actual/ Estimated Revenue</i>
1994-2000	\$ 176,157,390
2001	31,865,368
2002	34,797,562
2003	36,179,680
Total	<u>\$ 279,000,000</u>

Estimated revenues for FY 2003 is a variable number that forces the total amount to \$279,000,000. Assessing the 1/10th Mill for an additional full year would generate approximately \$37.3 million in additional revenues (assuming a 3% increase in the tax base from 2003 to 2004).

The Office of Counsel reviewed this issue in May 2000 and rendered the following opinion:

"The EFA, Not the Revenue Assumptions in Conceptual Design, Governs ECP Financing. The financial problems facing the ECP are generated, in part, by interpretations of the February 15, 1994 ECP Conceptual Design. That document estimated project revenues from the 1/10th millage at \$279 million. Although the Conceptual Design was incorporated by reference in the EFA, it is incorporated through Section 2, which defines the Everglades Construction Project, expressly referring to engineering concepts such as construction and operation schedules. The financial schedules and funding mechanisms in the Conceptual Design, however, were not incorporated into the EFA. Instead, the EFA established alternative funding mechanisms, authorizing the 1/10th millage point, the Agricultural Privilege Tax, and Special Assessments. None of these provisions refer to the Conceptual Design. In fact, since the EFA, Section 9(j) provides clear flexibility to District staff to modify the Conceptual Design to implement superior technologies, to achieve design objectives, and based upon standard engineering practices, the financial assumptions in the Conceptual Design must be equally flexible -- and indeed, the EFA states that the District shall take all reasonable measures to complete timely performance of the EFA. . .

The EFA Does Not Cap Revenues from the 1/10th Mill. It is important to note that District staff have previously used the \$279 million assumption in the Conceptual Design as a limitation on revenues from the 1/10th mill, and currently plan to terminate the millage in 2004. This self-imposed cap is a policy decision, however, because the EFA does not codify this limitation. Instead, **the 1/10 mill can continue to be collected in excess of \$279 million -- provided that the money continues to be used only for design, construction and land acquisition for the ECP [Emphasis added].** A decision to continue collecting the 1/10th mill could resolve the ECP cash flow problems, and substantially increase available revenues (as much as \$31 million each year). [Current estimate is \$37.3 million.]

Extending the Use of the 1/10 Mill to Other EFA Projects Will Help With Other Unfunded Mandates. Staff also noted that the ECP is not the only project required by the EFA, which also requires the District to obtain the Non-ECP and Long-Term Compliance Permits -- which ultimately requires the District to achieve compliance with all water quality standards at all discharge points into the Everglades. Although the EFA does allow special assessments, no general funding mechanisms were provided for these Non-ECP projects, such as the S-9/C-11W critical project being implemented by the Everglades Stormwater Program. District staff may consider seeking legislative changes to the EFA, allowing the 1/10 mill to be collected for other District projects required by permits issued pursuant to the EFA."

Although the current estimates project for the 1/10th mill to end in FY2003, the Agricultural Privilege Tax and Alligator Alley Tolls excess revenue continue through FY2014 to fund Operations & Maintenance expenditures. The revenues from these sources are projected to exceed operation and maintenance expenditures by a cumulative amount of \$21.5 million between FY2007 and FY2014. This amount is sufficient to cover the projected capital expenditure shortfall but is not sufficient to fully fund the additional two 298 District projects. Furthermore, this amount was calculated assuming that no interest expense is charged by the District's other funds to support the project during the deficit balance period after FY2006. The interest cost would amount to \$2 million between FY2007 and FY2014. In addition, after FY2014 the Agricultural Privilege Tax revenue drops by 60% and after FY2016 the Alligator Alley Tolls excess revenue source will end, which will result in insufficient revenues to fund the perpetual operation and maintenance cost.

Recommendation

4. **In the event that other revenue sources are not identified and sufficient additional savings are not realized on current project costs including operations and maintenance, we recommend that staff obtain Governing Board approval for assessing the 1/10th Mill Ad Valorem Tax for the length of time necessary to generate sufficient revenue to cover the current projected budget deficit and fund the remaining 298 Districts' projects.**

Management Response:

Heretofore, 2014 has been the year to reconcile the budgetary balances of the EFA directed construction. Any recommendation for extension of 1/10th mill should recognize this date as the previously established base in presentations to the Governing Board and legislative committees. Also, the "polluter pay" issue is a legislative concern and should be addressed prior to consideration of Recommendation #4.

Responsible Division: ECP Department

Estimated Completion Date: December 2002

5. **District budget and financial statements for ECP should be modified to include the full cost of the project including the remaining 298 Districts' projects.**

Management Response:

The funding for the 298 Districts was limited in the EFA, "...to the extent that funds are available from the Everglades Fund." The previous cashflow projections considered this provision of the Act. The ECP will provide an alternate cashflow projection including the construction component of the remaining two Chapter 298 District projects. The current cashflow statement (Oct 2001) includes an allowance (approximately \$1.3 million) for pre-construction activities to keep these two projects on schedule.

Responsible Division: ECP Department

Estimated Completion Date: January 2002

South Florida Water Management District

Schedule of Actual and Estimated Cost for 298 District Projects and Budget Shortfall

Projects	Cost Component				Total
	Land (2)	Construction	Engineering	Legal & Admin	
Substantially Completed Projects (1)					
East Beach Water Control District	\$ 1,106,183	\$ 4,208,968	\$ 1,176,477	\$ 146,541	\$ 6,638,169
East Shore Water Control District	679,766	5,679,520	902,809	114,742	7,376,837
Closter Farms	-	1,001,294	255,273	286,010	1,542,577
Subtotal Substantially Completed Projects	\$ 1,785,949	\$ 10,889,782	\$ 2,334,559	\$ 547,293	\$ 15,557,583
Actual Cost Incurred - Unfunded Projects (4)					
South Shore Drainage District	\$ -	\$ -	\$ 53,637	\$ 25,923	\$ 79,560
South Florida Conservance District	-	-	105,271	38,391	143,662
Cost Incurred for Unfunded Projects	\$ -	\$ -	\$ 158,908	\$ 64,314	\$ 223,222
Total - Funded	\$ 1,785,949	\$ 10,889,782	\$ 2,493,467	\$ 611,607	\$ 15,780,805
Unfunded Projects (3)					
South Shore Drainage District	\$ 284,593	\$ 1,759,151	\$ 217,266	\$ 91,700	\$ 2,352,710
South Florida Conservance District	455,873	5,145,791	362,531	123,124	6,087,319
Total - Unfunded Projects	\$ 740,466	\$ 6,904,942	\$ 579,797	\$ 214,824	\$ 8,440,029
TOTAL PROJECT COST	\$ 2,526,415	\$ 17,794,724	\$ 3,073,264	\$ 826,431	\$ 24,220,834

(1) Estimated cost as of September 30, 2001

(2) Includes appraisal costs

(3) Estimated cost to complete

(4) Represents actual cost incurred prior to suspending project

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REPLY TO: *WEST PALM BEACH*

VIA FACSIMILE
(561) 682-5398

October 23, 2001

Mr. Allen Vann, Inspector General
Office of the Inspector General
South Florida Water Management District
3301 Gun Club Road
West Palm Beach, Florida 33406

Re: Draft Audit Report: Audit of the Everglades Construction Project
Cooperative Agreements - Audit # 01-14

Dear Mr. Vann:

The following comments are submitted by East Beach Water Control District and South Florida Conservancy District (298 Districts) at the request of the South Florida Water Management District ("District") and are in response to draft audit number 01-14.

The audit is of the agreement entered between the 298 Districts, Closter Farm and the District under the Everglades Construction Project (ECP) to fund, design and construct diversion projects called for by the Everglades Forever Act (EFA). The audit is made at a point when two of the 298 District construction projects are nearing completion and two remain to be designed, funded and constructed under the agreement.

In sum the cooperative agreement calls for the District to fund and the 298 Districts to design and construct (with review but not approval power from the District) the diversion

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Mr. Allen Vann, Inspector General
October 23, 2001
Page 2

projects required under the EFA. The 298 Districts are then charged with meeting the cost and responsibility for operating the projects once they are constructed.

The purpose of the audit is to "substantiate expenditures submitted to the District for reimbursement, determine whether agreement provisions were complied with, and that best business practices were employed to obtain the greatest value for the taxpayer" with regard to the two nearly completed projects. The report also addresses the status of funding for the remaining two diversion projects contemplated as part of the cooperative agreement. Initially the audit concludes, and the 298 Districts agree, that all expenditures made by the 298 Districts under the contract were appropriate.

The audit also concludes that in the course of administering construction under the contracts there were opportunities missed to reduce professional fees incurred for engineering, appraisal and legal fees. Specifically, the report concludes that appraisal and engineering fees for the EBWCD were higher than they should have been. The report suggests that future amendments to the agreement should provide for stronger District control and more active participation by District staff in contract administration for project construction. Specially, the audit suggests that a better practice would have been to require bid and bid procedures for awarding the engineering and appraisal contracts and provide the District the opportunity to review the procedures and resulting bids.

It should be pointed out that when the Cooperative Agreement was negotiated, District staff was of the opinion that they did not want to administer any aspect of the project construction, including exercising review or oversight responsibilities for the retention of professionals. To that end, the Agreement was structured as a straight payment between District and the 298 Districts based on work or services provided and the submission of invoices for payment.

It must also be noted that in one instance District participation in reviewing the bid procedures and package failed to prevent higher professional fees and delayed project completion. EBWCD solicited comment from the District when it received a bid on its construction contract that was significantly lower than all other bids received. The bid was from a contractor unknown to EBWCD staff or engineers. District staff, who had knowledge of the contractor and who had reviewed the bid, indicated that it was their opinion that the contract should be let to the unknown contractor. Contract completion has run over deadline by more than six months. The contractor, who proved unable or unwilling to complete the work, was defaulted and removed from the job site. Considerable additional attorney and engineering expenses were incurred as a result of the selection of this contractor. This does not suggest that District staff is responsible for the delay or overrun, but it is evidence that indicates District oversight on such matters is not necessarily a prophylactic solution.

Mr. Allen Vann, Inspector General
October 23, 2001
Page 3

It might also be suggested that in the event similar difficulties arise and the District has determined to take a more active role in letting of the contracts and in construction management, it will also need to include in its budget funds necessary to pay attorney's and engineers to defend or prosecute any breaches of the construction agreements.

The 298 Districts also disagree that engineering contracts should have been bid for the construction of the projects called for in the agreements. Section 298.16, Florida Statutes, provides for appointment of a District Engineer by the Governing Board of a 298 District. This appointment was made many years prior to initiation of the Diversion Project and execution of the Cooperative Agreement. At that time, the District Engineer selection was subject to Florida law, the Consultant's Competitive Negotiations Act.

Additionally, and perhaps more important, the District Engineer was originally involved directly with the Department of Environmental Protection (DEP) and the District in the design of the Diversion Project. That design is incorporated in Consent Agreements between the 298 Districts and the DEP whereby the 298 Districts are obligated to implement diversion. It is, therefore doubtful that, under any circumstances, engineering costs would have been any more economical had they been subjected to additional competitive solicitations. The District Engineer was not only involved in the Diversion Project long before the Cooperative Agreement was executed, the District Engineer was directly involved in the design of the Everglades Construction Project before it was enacted into State law.

The 298 Districts believe that the appraisal fees incurred were also reasonable given the particular circumstances of the completed projects. The 298 Districts did use an appraiser approved by the District and knowledgeable of Everglades land values. The appraiser took on an additional role of negotiating for the purchase of the land interests necessary to complete the projects. This resulted in larger appraiser fees but lower overall professional costs. Use of a knowledgeable and credible appraiser allowed the project to proceed without initiating any condemnation litigation.

Finally, the 298 Districts agree with the funding projections contained in the audit, with the understanding that they have not undertaken to render an independent analysis of the remaining funds required to complete the projects which are part of the ECP. The 298 Districts agree that the original funding estimates were based upon outdated revenue projections. The 298 Districts do not object to the suggested means of obtaining the additional funding required to complete the projects i.e. extension of the 1/10 mil ad valorem tax as permitted by the EFA for an additional year beyond the original projection.

Mr. Allen Vann, Inspector General
October 23, 2001
Page 4

Thank you for your consideration of this response.

Sincerely,



Kevin S. Hednessy

KSH/caj

c. Howard Searcy, P.E. (via facsimile 561- 996-2960)
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October 23, 2001

VIA TELECOPY AND U.S. MAIL

Mr. Allen Vann
Inspector General
Office of the Inspector General
South Florida Water Management District
P.O. Box 24680
West Palm Beach, FL 33416-4680

Re: Draft Audit Report: Audit of the Everglades
Construction Project Cooperative Agreements
Audit # 01-14

Dear Mr. Vann:

This is in response to your letter dated October 3, 2001, to Modesto Ulloa of Closter Farms, Inc., forwarding a copy of the draft audit report of the Everglades Construction Project Cooperative Agreements, Audit #01-14. Closter thanks the District for the opportunity to provide comments. Since the purpose of your audit is to assess your internal systems and find ways of improving them, we do not propose to address your recommendations to your agency, but limit our comments to those aspects of the report that we believe should be clarified as they relate to Closter and Closter's contract with the District.

A preliminary note: With respect to Closter, the draft audit report makes several references to the relatively high proportion of professional fees in comparison with construction costs. As discussed in more detail in the specific comments below, there were three factors unique to Closter that explain that higher proportion:

Mr. Allen Vann
October 22, 2001
Page Two

(1) The economies of scale that were available to the 298 Districts, whose construction projects were several times larger than Closter's, were not available to Closter; thus, because the legal work for Closter's single project was for the most part the same as the legal work for the 298 projects, Closter's legal fees were proportionately greater.

(2) Closter's project required additional legal work that was not needed by the 298 Districts, including an easement from the Trustees and the School Board, and landowner agreements from landowners in the basin that were beyond Closter's control.

(3) Closter is a farming company, and as such it does not maintain an in-house staff to handle government construction projects. Nevertheless, Closter completed the project within budget.

In assessing the implementation of this contract, it is important to be aware that the enabling legislation (the Everglades Forever Act) resulted from the hard work, willingness to cooperate, and compromise of many and diverse interests. The idea that a farming company such as Closter Farms would be directed by statute to build a diversion project to be reimbursed with District funds, is relatively unprecedented. The contract between the District and Closter cannot be compared or even judged with the same standards as a typical District procurement project.

Our comments below are keyed to pages of the draft audit report and follow the order of the report. At the outset, we have a general comment applicable to the entire report: The draft audit report addresses both the 298 District contracts and the contract with Closter. Some comments are addressed to all the contracts, others to matters specific to the 298 Districts or Closter. While there are specific portions of the report addressing both entities, and are so identified, the general comments include portions that are applicable to one entity or the other, but it is not always clear to us which entity was intended. When you prepare the final audit report, we recommend you clarify any such ambiguities.

Mr. Allen Vann
October 22, 2001
Page Three

Introduction, Page 3:

The draft audit report Introduction summarizes what are described as the primary obligations of the 298 Districts' cooperative agreements, and then states, as to Closter: "Similar provisions are included in the Closter Farms contract." While this is generally true, we call to your attention two significant differences between the quoted sections of the 298 District agreements and the SFWMD contract with Closter:

(1) Article II, Section B -- Unlike the 298 District agreements, the Closter contract did not provide for District review of and comment on the solicitations for engineering contracts. This is especially significant because later in the draft audit report, the comment is made that the District was not afforded the opportunity to review engineering contracts. The District did not require review and comment on solicitations for engineering contracts in the Closter contract because it reviewed and pre-approved the use of the Closter Engineer of Record. The use of this engineering firm was included as a condition of the contract, which also included a budget for the engineer's services.

One of the things that made this legislation unique is that extensive consultative work was done by Closter's engineer before the legislation was enacted. Closter's engineer provided assistance to Closter in review of the Everglades Construction Project, which was adopted by reference in the legislation. The 298 Districts' engineer was likewise involved in consultative work for the Districts. The knowledge gained by the engineers in this process, both those of Closter and the 298 Districts, was invaluable later in keeping down the reimbursable engineering costs of the projects. We expect that the 298 Districts, like Closter, benefited tremendously from being able to use the same engineering firms that provided consulting services before the contracts were signed. Those costs incurred by Closter in reviewing the impact of the Everglades Forever Act were never claimed nor reimbursed, but the benefit of that experience, and the engineer's years of working the property as a consultant to Closter, would have been lost if a new engineering firm had been introduced into the picture. We

Mr. Allen Vann
October 22, 2001
Page Four

believe the District recognized this when it accepted the engineering budget in the Closter contract.

(2) Article V, Section A -- The Closter contract did not have a section analogous to Article V, Section A of the 298 District Agreement. The District reviewed the concept of using an escrow agent for the Closter contract but opted for the reimbursement format instead, so no escrow account was involved or necessary.

Results in Brief; Review of Costs, Page 4:

In your review of costs, you indicate there were opportunities to reduce professional fees incurred for engineering, appraisal, and legal work. You also contrast Closter's professional fees (54% of construction costs) with those of the 298 Districts (23% of total infrastructure costs) and note that many legal fees were actually project management fees for services that could have been rendered by others. While we respect that this is your opinion, Closter suggests that:

(1) The use of the team selected by Closter, resulted in significant savings because of the experience the members brought to the project, as detailed above. If we, as a regulated entity, have a criticism of the process, it is that it took 3 years to finalize this contract after the Everglades Forever Act was enacted.

(2) Closter is a farm company; it is not a contractor that submits bids for its work, nor a governmental entity experienced with managing bids and bidding procedures for government projects. It is to be expected that a reimbursement contract with such an entity would provide for accounting, legal, or engineering assistance that might not be necessary for a governmental agency or ordinary bidding contractor with its own in-house staff. Closter was committed to handling this matter in a professional and well-documented manner, and for this reason hired the team necessary to accomplish this, including an independent accounting firm.

Mr. Allen Vann
October 22, 2001
Page Five

(3) Closter kept a separate billing account for any "project management" type activities conducted by its legal firm. Those activities were billed and paid for by Closter individually. The District was never billed for those services, and we disagree that legal services billed to the District included project management type activities.

Review of Accounting Records and Payment Process, Page 4:

The draft audit report indicates that vendor payments were made in accordance with executed contracts and no questioned costs were identified. We are not sure what you mean by that statement, but District staff did question some of the legal costs claimed, and some such costs were disallowed by staff. We had no doubt that our bills were being carefully scrutinized by District staff, who asked plenty of questions about billed items. Those disallowed costs were absorbed by Closter, together with the project management costs mentioned above that were not billed by Closter to the District.

The draft audit report mentions that "District staff did not maintain adequate supporting documentation for reimbursements made during the first two years of the contract." Closter did provide detailed invoices to the District throughout the process. As previously stated, District staff did question various items billed, so somewhere in the process they did review these reimbursement requests with a fine-tooth comb.

Compliance with Contractual Requirements, Page 5:

The draft audit report indicates that District staff was not afforded the opportunity to review and comment on solicitations for engineering contracts. As noted above, this was not a requirement of the Closter contract because the contract actually approved of the terms for engaging the engineer and the engineer's budget. Moreover, Closter did provide a copy of the contract to the District for review prior to execution.

Mr. Allen Vann
October 22, 2001
Page Six

Everglades Restoration Project Funding Issues, Page 5:

In this section, the 298 Districts and Closter are lumped together in a statement that the "projects are currently estimated to cost approximately \$12.7 million more than the ... original estimate." We call to your attention the fact that Closter completed its project within budget. Closter requested and was granted a contract amendment of only \$150,000. Some of these costs resulted from the extensive peer review conducted by the District's contract engineers. This peer review required responses from Closter's engineer, which had not been envisioned in the contract. Another unanticipated cost was acquisition of an easement needed for the project. It had been contemplated in the budget that the District would do this work. Closter's attorney had to do it instead.

Findings and Recommendations, Review of Costs, Closter Farms, Pages 9 and 10:

The draft audit report indicates Closter Farms's professional fees were 54% of construction costs. As noted above, Closter is a private farming concern; it is not a contractor or a governmental entity. The legislature chose to have Closter build this project. It should be expected that a farming enterprise would not have the in-house capability to do this kind of work.

Note 1 states that no land interests were required for Closter. This is incorrect. Closter had to secure an easement from the Board of Trustees of the Internal Improvement Trust Fund and the School Board of Palm Beach County. This is not recognized in your report as one of the services rendered by our attorneys. There were no land costs associated with obtaining this easement, but there were legal fees associated with the process. As noted above, it had been envisioned in the budget that the District would do this work, but we were later advised that Closter had to do the work itself.

Mention is made in Note 3 that the engineering fees were just above the benchmark. Please be aware that the fees would have been closer to the benchmark were it not for the extensive

Mr. Allen Vann
October 22, 2001
Page Seven

peer review process that was interjected in the project without prior indication that this should be built into the contract budget.

In Note 5, the draft audit report makes some comparisons between the legal services costs versus total project costs in the 298 District contracts and the Closter contract. The fact that Closter's legal fees were significantly higher is attributed in the draft audit report to the "project management activities" of Closter's counsel. Please see our comments above regarding this point. In the listing of legal services rendered elsewhere in the report, mention is not made of legal services required for easement acquisition.

Further, the draft report did not recognize that the construction budget for the 298 Districts was significantly larger than Closter's, so the relative percentages of legal costs vs. project costs would be disparate. The legal work involved in the project did not increase just because the construction project size was bigger; that remained constant whether there were 4 projects or one. The economies available to the 298 Districts, with their larger projects, were not available to Closter.

The 298 Districts also did not have to negotiate landowner agreements with parties located within their basin in order to obtain requisite permits. Closter was in a unique situation because it was responsible for planning and executing a diversion project that included lands beyond its control. Negotiating landowner agreements with the City of Pahokee, the School Board, the Palm Beach County Airport, and the Board of Trustees of the Internal Improvement Trust Fund can hardly be considered "project management" that a low-level engineering firm employee could accomplish successfully in lieu of using a lawyer.

Conditions Affecting Costs, Page 10:

First Bullet -- Please note the above comments relative to the statement that the District was not involved in soliciting or negotiating contracts for professional services.

Mr. Allen Vann
October 22, 2001
Page Eight

Second Bullet -- Please note the above comments relative to the statement that higher-priced professionals were used to provide services that required skills that could have been provided by lower-priced professionals. As to the comment about legal fees, please note that Closter used a legal professional who worked for Closter under this contract -- at the specific request of District staff -- at a reduced rate, which rate was deemed commensurate with similar rates paid by the District for its own outside counsel.

Third Bullet -- Please note the comments above relative to the statement that the agreements obligated SFWMD with the responsibility to pay for the projects without the authority to manage cost. As stated above, costs were thoroughly managed and reviewed by District staff. Staff was faced with a unique legislative enactment and integrated District project management notwithstanding circumstances that were out of the ordinary.

Recommendation 1, Page 12:

See comment above regarding questioning of vendor payments. In this section, the draft audit report states: "... District staff did not receive, review, and maintain adequate supporting documentation for reimbursements made during the first two years of the contract(s). Most of the cost during this period was for legal and engineering services, for which summary invoices were provided for amounts paid; however, documentation was not provided to support the charges from the vendors." Please note that no charges were ever submitted to the District by Closter that were not documented, and legal services, which were most of the referred-to initial costs, were heavily and specifically documented (daily descriptions were provided for all work, with detail down to the quarter hour).

Recommendation 2, Page 13:

Please see the comments above relative to opportunity to review professional services contracts and our opinion relative to savings achieved by using firms familiar with the project.

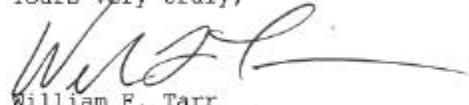
Mr. Allen Vann
October 22, 2001
Page Nine

Recommendation 3, Page 14:

We would appreciate the clarification that the cost overruns described in this recommendation do not apply to Closter.

Again, thank you for the opportunity to comment. Please let me know if you would like further information. With best regards, I am,

Yours very truly,



William F. Tarr
Vice President and
Legal Counsel
Closter Farms, Inc.

/jw

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